INTERNATIONAL HELLENIC UNIVERSITY

Towards a European Banking Union: the European Deposit Insurance Scheme

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SCHOOL OF ECONOMICS, BUSINESS ADMINISTRATION & LEGAL STUDIES
A thesis submitted for the degree of
Master of Laws (LLM) in Transnational and European Commercial Law & Alternative Dispute Resolution

February 2018
Thessaloniki – Greece

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February 2018
Thessaloniki - Greece

Abstract

This dissertation was written as part of the LLM in Transnational and European Commercial Law & Alternative Dispute Resolution at the International Hellenic University.

The European Banking Union was proposed by the Commission in 2012 as a portion of the long-term mission for fiscal integration aiming at the restoration of confidence in eurozone. The plan was intended to be implemented gradually with a shift of the banks' supervision to a European level, with an establishment of a common framework responsible for crisis management as well as with a shared system for deposit insurance. The first two measures have been implemented so far but the third measure remains the missing pillar of such a Union. A backed European Deposit Insurance Scheme would be the best protection that could be added to the national deposits guarantee structures which are estimated €100,000 per account and bank.

I would like to thank my supervisor, Dr. Thomas Papadopoulos, for his excellent guidance and support during this process. I also wish to thank all of the respondents without the cooperation of whom I would not have been able to conduct this analysis.

Keywords: European Banking Union, Deposit Insurance Scheme

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February 2018

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Introduction

It is widely known that the financial system in Europe is dominated by banks, as they are the structures which offer the majority of credit to enterprises and households. It is expected that they can ease investment and financial development. Up to the previous years, the banking system of each European Member State was supervised and regulated only at a national level, but according to the recent developments during the financial crisis, these arrangements were found not to provide satisfactory steadiness in the financial system.

A "European Banking Union" seems to be the finest solution for the fiscal system's weaknesses. According to Gros and Shoenmaker (2014), such a union would provide the best desirable outcomes in the financial system. Firstly, the systemic risk will be reduced. In national banking, the focus is on national interests and the joined value of banks is ignored, while a "Banking Union" would absorb the potential failures of the system at a European level. Furthermore, a Banking Union could separate national governments from the banks, as it would include a safety net guaranteeing the solidity of the structure independently from any national weaknesses. It could act as a mechanism which both shocks the system and absorbs its failures and succeed in preventing potential failures by appropriate regulation or even managing a potential crisis.

A unified banking system requires single bank supervision, single bank resolution and single deposit insurance. While the two pillars of the European Banking Union are in place (single supervision and single resolution), deposit insurance still remains national. Although proposals for the centralization of deposit insurance were made many years ago, it became a hot topic during the Eurozone crisis; IMF published a paper in 2010 anticipating a unified European deposit insurance system and European Commission finally issued a proposal for a Regulation establishing a European Deposit Insurance Scheme (EDIS) in 2015. Since then very few steps of progress have been made, while the proposal has been highly criticized and raised many political debates in the EU.

The aim of this paper would be to examine the “Single Supervisory Mechanism” and the “Single Resolution Mechanism” along with their legal framework and then focus on the proposal of the European Commission regarding the “European Deposit Insurance Scheme”. Its purposes, the steps of its enactment as well as the advantages and disadvantages related to it would be taken into consideration in order for the concept of EDIS to be fully understood, since it is a significant area which bothers the European Community.

The European Banking Union

The Banking Union is a key element of the European Economic and Monetary Union (EMU) and is a step of high significance towards financial integration in Europe. As stated in Five Presidents' Report "Completing Europe's Economic and Monetary Union" (June 2015) "A single banking system is the mirror image of a single money.”

The principles of the establishment of a Banking Union

Looking back on the recent European banking history, there are many indicative cases where the lack of a real Banking Union proved to be inefficient. The case of Fortis, an important bank for both the Netherlands and Belgium, is an example indicating the failure of the national states’ co-ordination especially during a financial crisis. After the economic crisis of 2008 broke up, Fortis was highly affected. However, national interests of each State preceded the European ones regarding the approach proposed so as to save Fortis (Berck, 2012). With the local parliaments guiding political choices for both counties, Belgium wanted to save the whole bank and keep its base in the capital of Belgium while the Dutch government wanted to divide the bank. In this instance, a federal alternative solution should have been required, since a unified market such as the European has the potential to absorb the systematic consequences of banking failures.

A further issue in European Union is the impact of the stress of one of its members to the whole banking system. For instance, Ireland is a case where domestic real estate market led to significant losses which could not be covered by its national sovereign and its national deposit guarantee system. According to Gros (2012) Ireland share some important features with Nevada, such as the size of their population and the strong flourishment of their real estate market. However, when the market stopped flourishing, Nevada and Ireland experienced the crisis differently as in United States banking system issues are solved at a federal level whereas in the European Union banking problems used to remain the responsibility of the national states. This is an indicative example of the different results of each approach. In Nevada, the banks’ failures were seized by the Federal Deposit Insurance Corporation which absorbed the losses and gave the operations to banks that were more powerful. An equivalent banking system in European Union could have rescued Ireland's banking system (Grow & Shoenmaker, 2014).

Hence a national deposit guarantee system created by the eurozone could not only offer a mechanism which absorbs external losses, but it would be totally independent of the national sovereign. Thus, a mechanism like that would be very important during an economic crisis eruption as it could prevent the deep recession, the creation of uncontrollable deficits and the public debt's growing levels.

Crisis management

Countries have had certain mechanisms which helped them lend the insolvent banks. However, it could be possible that problematic banks exceeded the available resources. In this case, central banks would have to lend money even when their role is just to lessen the risk. Thus, the European Central Bank could not be the appropriate institution to become the lender of the last minute as it could not fully control the banks which used to be managed by the national government. There were problems of coordination which had to change, and this could be done only within a "Eurozone Banking System". Authorities have to be informed about the money needed to avoid their banks' failure because money of the taxpayers is included. The viability of a failing bank must be considered and in case of an emergency it would be better that problematic banks shut down in order to reduce the impact on the deposits.

As bank crises were tending to explode and spread throughout the whole fiscal sector, it became obvious that the decisions should be quick and the authorities should be prepared and well informed. Many developed states had already created institutions which had the role of the supervisor and resolution authorities which had the responsibility to restructure the bank or shut them down in case of failure. In the case of Eurozone countries back then, it used to be one central bank but no supervisor (Wyplosz, 2012).

The benefits of a Banking Union

The Banking Union is an idea that appeared in economists' discussions many years ago, but it was after the last financial crisis that it was moved up. However, despite the wide acceptance of it as a necessity for the future of eurozone, it was not clear from the beginning what exactly a "Banking Union" would be and how it would function within the Eurozone. Nonetheless, authors agreed that there would be a union with a central supervision- as the national supervision worsens the situation- and it was considered to be part of a package with reforms associated with the entanglement of banks with sovereign. Additionally, it was implied that there would be long-term reforms which would address the sovereign fragility.

According to the "Five Presidents' Report", a Banking Union is a central movement towards the implementation of an Economic as well as a Monetary Union which will have the capacity to offer a more satisfying life to EU residents. The basic mission of such a union is to stop the association between states' banking systems and their taxpayers. In this way, a failing banking system would not be able to influence negatively the public debt and vice versa.

One of the most important benefits of a Banking Union will be the protection against instability of banks. "Deposit Guarantee Schemes" are designated to protect individuals from bank bankruptcy and in this way, eliminate the possibility of general bank runs which were significant during the last financial crisis. Nevertheless, current "Deposit Guarantee Scheme" is exposed to instability because of its national character. A common insurance scheme would have the potential to increase flexibility against possible crises in the future (Nouy, 2016). Therefore, it was proposed by the five President's report to establish a "European Deposit Insurance Scheme" as a pillar of a settled Banking Union.

An additional benefit of the Banking Union is the reduced consequences of a bank failure for taxpayers, since a shared euro scheme is likely to be financially neutral and not national as with Deposit Guarantee Schemes. For this measure to take place, it is imperative to determine the minimum amount of officially required national deposit insurances and then proceed to the design of cross-country ones. A very influential aspect of a common Scheme would be the independency of it from state's policies.

Nonetheless, this feature may create issues with incentives as a common liability attracts officials to dump costs on other countries (Schoenmaker et al, 2016).

Finally, it is imperative to be defined whether the Banking Union would be just for the Eurozone or for all countries which participate in the European Union. According to Beck (2012), the need for a unified banking system is much more intense within the currency union as there is tight association between the fiscal and monetary stability. This is impaired by national authorities which do not possess the necessary tools that countries with monetary independency already have. However, it appears that non-eurozone countries could participate in the Union, but they would not have the same benefits and responsibilities that the members of the eurozone have. In general, it is stressed that there is a need to involve all banks, even small ones. In this case, European Central Bank would be the creditor of the last minute for the whole banking system but it would have the right and responsibility to resolve and supervise all the banks of the union (Beck, 2012).

The risks of a Banking Union

The urgency for the creation of a Banking Union came from the idea that a safety net for Europe was not complete. The European Central Bank has become the main lender although it has inadequate information about national banks. Also, national governments tend to recapitalize their banks admitting more and more pressure to the European Central Bank to take measures (Beck, 2012).

On the other hand, the ECB's dual role includes conflicts of interests. For instance, financial policy and steadiness measures are significantly in accordance but there is a potential risk associated with the fact that the ECB will be the sole liquidity provider. Furthermore, there are risks concerning the potential conflicts between the two domains of activity of the Central Bank and the legal risks which permit some kind of scrutiny (European Central Bank, 2013).

The two main pillars of the European Banking Union

The Single Supervisory Mechanism (SSM) along with the Single Resolution Mechanism (SRM) is established as the two main pillars of the “European Banking Union” providing single supervision and single resolution.

The Single Supervisory Mechanism (SSM)

The Supervision of the credit institutions within the Eurozone is substantial as it helps restructure the trust within the banking sector and ensure the flexibility of the credit institutions. The last fiscal crisis depicted how fast and intensely can financial problems spread within a monetary union and how crisis can affect the citizens of Eurozone countries.

The purposes of the SSM are to shield the European banking institutes, upsurge fiscal unity and solidity and guarantee steady management. It has the ability to make the banking sector more integrated and offer a risk-orientated and balanced supervisory style.

The SSM consists of the banking supervision structure which comprises of the ECB and the National Supervisory Authorities which partake in the Eurozone.

The function of the ECB would be to establish an approach which is the same for all members maintaining a balance between the measures that it takes and the supervisory activity and ensuring that the regulations and policies apply consistently to all members. Its main responsibility is the direct supervision of important banks of the countries which are members of the Eurozone. The criteria according to which a credit institution is considered significant are associated with its size, financial importance, cross-border assets/liabilities, financial assistance, etc. Moreover, the ECB is authorized to accomplish supervisory evaluations, inspections as well as investigations, provide or revoke banking licenses, evaluate banks’ qualifying holdings, make sure the banking institution comply with the European Union rules and set higher buffer to avoid fiscal risks.

Comprehensive assessment is one more function of the Central Bank which advances its supervisory tasks. According to its additional role, the ECB will assess the banks in order to achieve a greater transparency of their functions and expand the information about them that becomes available. The aim is to build confidence. There are three aspects which are fundamental. The first is the assessment of risks like liquidity and funding, the second is to ensure the exposures of the bank such as the quality of assets that involves and the last aspect is the stress test which investigates the balance sheets of it in case of risk (ECB Press Release, 2013).

The access to the expertise of the Central Bank has the potential to ensure the quality of the processes associated with decision-making and increase the effective outcomes of the mechanism. The supervision will not be provided freely as the banks will be charged with fees (European Central Bank, 2013).

However, the effectiveness and consistency of the Supervision of the European credit institutions are not safeguarded only by ECB; collaboration of it with the National Supervisors of the participant states is required. There are credit institutions- that are considered less significant- which are supervised indirectly by the national authorities, though in tight cooperation with the Central Bank.

The countries which partake automatically in the SSM are those of Eurozone while other countries of the European Union can either participate or not. However, if they want to participate, the national supervisors have to tightly cooperate with the ECB. If there are countries which do not take part in the SSM, then a memorandum clarifies the cooperation of the Central Bank with the countries' national supervisors on aspects of their credit institutions' supervision (European Central Bank).

The successful implementation of the SSM will ensure that the banks will be protected by eliminating the national bias. Thus, the implementation of SSM depends on several actions such as the proper scoping of the jurisdictions of every Member State as all their banks will have to cooperate with the ECB and be supervised by it.

The SSM has as a basis the construction of a powerful center which has the support of ECB and where the tasks between the center and the periphery of it are adequately allocated. The Central Bank will be responsible for the function of the system but the operationalization of it will be the responsibility of the national authorities since they are closer to the banking institutions that are supervised as well as more expertise. When the Banks are supervised by the ECB directly, officers from the national authorities will be present in the inspections of the ECB. Hence, there would be joint teams representing both the ECB and the national authorities which will be responsible for the process (European Commission, 2013).

The financial crisis in the Eurozone area has reinforced the tendency of the banks which are supervised to benefit from the interactions between financial policy and management. The assignment of supervisory mechanisms to the ECB reflects the leading agreement in many national authorities. The benefits from the interaction of financial policy and managements stem from the distribution of information associated with the financial policy, the supervision of the credit institutions and the omission of payment mechanisms. Moreover, the significant banks can take advantage from the expertise associated with the analysis of financial stability and the independence of credit institutions which have evidently defined guidelines of liability and can have a positive contribution to the successful conduct of monetary stability processes.

The implementation of SSM started at the last months of 2015 when the “European Banking Institute” was established. EBI is a structure counterpart to the SSM and consists of a net of universities from the whole Europe. This institute gives the change to the academic and professional world to meet and share their views about the legal procedures behind SSM and EBU.

An important advantage of the whole process is the contribution of SSM in the upgrade of a Single Market, where all European banks take part recognizing the limitations of each national law. The legal framework aims to balance the way the SSM works.

However, national differences have been the main issue behind the establishment of a “balanced legal and regulatory framework by the European Commission” and the “European Banking Authority (EBA)”. There are supervisory procedures which are regulated by national law. For instance, the “Capital Requirements Directive” is a mechanism allowing the Member States to select the way and the process of implementation. Thus, there are provisions of it that function in a different way for each member.

Unfortunately, there are countries where non-compulsory supervisory procedures within compulsory legal acts existed, therefore making it more difficult for the Central Bank to balance these procedures. An illustrating example is associated with German law which regulated the resolution of credit institutions. According to it, the Ministry of Finance had still the authority to establish regulations like risk management (European Commission, 2013).

According to Lautenschläger (2016) the regulatory procedures in Eurozone area displayed an image of fragmentation, but national law has not the right to differentiate from SSM. If there are different supervisory styles, then the two styles (the national and the European) have to merge in a way that the whole process would function appropriately. A consistent style and a common rulebook are the landmarks which can help the system to work sufficiently.

The Single Resolution Mechanism (SRM)

However, the SSM cannot function alone; it needs to be supplemented by the SRM in order to provide its services to credit institutions that are not viable. Otherwise, the SSM may encourage a type of supervision that has its basis on the expectations of the ECB associated with granting liquidity. It would not be possible to avoid having banks which are in trouble. Thus, an SRM is needed to make sure that credit institutions that are not viable will be resolved (European Central Bank, 2013).

According to the decisions of the European Commission, the Single Resolution Mechanism is a central organization for the resolution of credit institutions within the European Union and one of the two pillars of the European Banking Union. The term resolution refers to the reorganization of a credit institution by a resolution mechanism when it is about to fail. This mechanism makes sure that the failure of the credit institution would not spread or influence negatively the broader financial system or cause any kind of fiscal instability.

The Single Resolution Mechanism can be applied only to institutions which are supervised by the European Central Bank and therefore, are protected by the Single Supervisory Mechanism. In the case where a credit institution that has received the supervision of the Single Supervisory Mechanism fails, the Single Resolution

Mechanism gives the chance for its resolution to be managed through a Single Resolution Board and a Single Resolution Fund which is financed by the wider banking sector.

The aim of the Single Resolution Mechanism is to protect taxpayers and the European economy from the possible costs that a failing credit institution could bring. This measure is associated with the fiscal crisis which broke out in 2007-2008 and spread around the world affecting taxpayers and governments whose credit institutions were failing as there were not any resolution and crisis management frameworks for similar situations. These developments following the fiscal crisis suggested that a different approach was mandatory for the management of the banking sector's crisis and the provision of a fiscal stability (European Commission, 2016).

The Regulation (EU) No 806/2014 which establishes the Single Resolution Mechanism creates a framework for the resolution of the credit institution within the European Union. The most important authority established by the above Regulation is the "Single Resolution Board" which acts as an autonomous resolution mechanism within the European banking sector. The Single Resolution Mechanism is composed by the Single Resolution Board and the states that participate in the Eurozone. The aim of the Single Resolution Board is to safeguard the European economy and the citizens' credit from the failing credit institution within the European Banking Union and accomplish the "Single Resolution Fund" (European Commission, 2015).

It is critical to protect the temporary and impartial decisions that are taken by the national authorities in these situations. The SRM has the potential to ensure that taxpayers will not pay for the preservation of non-viable banking institutions as in an economy where the private market dominates, the credit institutions cannot be protected from closing if they are not viable. However, these procedures need to be orderly and not to be influenced by national bias. This mechanism must be placed within the Central Bank in order to avoid any upcoming conflict of objectives. From an institutional view, the SRM should follow the similar procedures with the SSM. The responsibility of the mechanism would be to govern the resolution of credit institution and coordinate the implementation of resolution apparatuses.

One of the most critical components of banking resolution is funding. Hence, there is a need for the establishment of efficient financial measures. In order to achieve this, a European Resolution Fund has to be established so as to offer the necessary funding when it is required. In case the resources provided by the above Fund are not adequate, then funding should be provided by the European Union back-stop mechanism (European Central Bank, 2013).

The Legal Framework behind SSM and SRM

The Single Supervisory Mechanism's establishment took place on 4/11/2014 and represented a fundamental step towards the Banking Union's establishment. A whole set of legal acts had to be adopted for the founding of Single Supervisory Mechanism in a short period of time. The involvement of the legal services of the Central Bank of Europe was substantial in the establishment of a series of Legal Booklets related to the legal framework of the Single Supervisory Mechanism. Particularly, the series of Legal Booklets encompasses the most important legal acts associated with the administration of the Banking Union together with other legal acts associated with other European institutions such as the Council regulation.

The Single Supervisory Mechanism Regulation includes the founding principles and general rules associated with the function of the Single Supervisory Mechanism. It also made clear which are the tasks of the European Central Bank in the area of supervision of banking entities. The Central Bank has the responsibility for setting the standards of supervision of the banking sector and collaborating with the national competent authorities. Furthermore, it sets the criteria for the determination of significance. In other words, it contains the methodology according to which a banking institution is determined as significant or not as well as the procedures underlying the cooperation between the Central Bank and the National Competent Authorities with a concern to which banking institutions are significant or not. Finally, it includes issues associated with the macro-prudential choices, close collaboration, investigatory supremacy, sanction, qualifying properties and authorizations.

Additionally, it provides for a Supervisory Board, which would be the internal body of the Central Bank and would be responsible for the design and execution of the

Central Banks' tasks. According to the Single Supervisory Mechanism' Regulation, it is imperative to adopt rules which set out the cooperation with the Supervisory Board. More specifically, the new rubrics create the relationship between the Supervisory Board and the Governing Council under a procedure called non-objection procedure. This procedure requires that the informal decisions of the Supervisory Board become official if the Governing Council does not object within a defined period of time.

Furthermore, the Regulation requires the adoption of Supervisory Board's specific Rules of Procedure. The Central Bank's and the Supervisory Board's Rules of Procedure were available on the Central Bank's site and published on Institutional Provisions, a separate legal booklet in June 2015. The Regulation founds an Administrative Board of Review set by the Central Bank of Europe which is charged with the responsibility for the formation of administrative reviews of the Central Bank's supervisory tasks' decisions. The Administrative Board of Review is responsible for the review of the decisions upon the Central Bank's request and it will consist of five experts with significant experience in the financial and banking services.

The Regulation establishes an additional internal body called the Mediation Panel with the aim to ensure the division between the supervisory tasks and the monetary policy. Additionally, this body will be responsible to deal with any opposition of the Central Council associated with the informal decisions of the Supervisory Board. The rules related to the decision of the Supervisory Board and the cooperation with the Governing Council are regulated by the legal services which are created by the Mediation Panel, the Administrative Board of Reviews and the rules associated with the separation of the Central Bank's function of monetary policy and its supervisory tasks.

There is also a procedure according to which there will be a chance for the Member States which are not in the eurozone to become members of the Banking Union. The decision encompasses the procedures related to the requests to cooperate closely with the Central Bank, the requests' assessment by the Bank and the assessment's outcome. Once cooperation is established, the Framework Regulation is responsible for the operation of the cooperation and the forms of supervision that is to be conducted (European Commission, 2015).

Regulation (EU) No 1022/2013

According to the Regulation (EU) No 1022/2013 the European Commission suggested a Single Supervisory Mechanism which encompasses the Central Bank of Europe. The President of the European Council -in association with the President of the Central Bank and the European Commission- was asked to develop a particular plan for the creation of a monetary and financial union which encompasses specific proposals related to the well-being of the fiscal services within the internal market. The primary phase towards the formation of the Banking Union within the Eurozone is the construction of a single supervisory mechanism supported by a single set of directions for the fiscal services as well as a novel basis for resolution and deposit insurance. Council Regulation (EU) No 1024/2013 provides the Central Bank with particular tasks associated with the practical supervision of banking institutions in the Members of Eurozone and permits the other Associates of the Union that are not in the Eurozone to form a tight collaboration with the Central Bank. Member States whose banking institutions are administered by the Central Bank should not hamper the function of financial services in the internal market. The Banking Authority of Europe should preserve its role according to the Regulation (EU) No 1093/2010 and maintain its current powers and responsibilities associated with the rules which apply to all Members of the Eurozone (European Commission, 2015).

Furthermore, the involvement of mechanisms of democratic accountability are critical as well as the insurance of the security and reliability of banking institutions. The Central Bank should be fully conscious for the multiplicity of banking institutions, their business models, their magnitude and the welfares associated with the diversity within the banking industry in Europe.

The promotion of the most effective supervisory practice within the market is essential to combine the single rulebook with the supervision of the credit institutions carried out by the Central Bank together with the National Competent Authorities. The supervisory handbook should find the most effective practices associated with processes and methodologies to accomplish adherence to central Union and international principles. This handbook should include all the tasks of the Central Bank's responsibility without taking the form of legal acts. These tasks might include:

the protection of the consumer, the money laundering's fight, the establishment of methodologies and metrics for the assessment of any risk.

Additionally, the Regulation establishes that the Central Bank of Europe could ask for information from the credit institutions associated with anything that is legally acceptable such as information held by people paid by these credit institutions to accomplish important activities, inspections provided to those credit institutions by outside inspectors as well as copies of significant books, records and documents.

Moreover, according to the Regulation the Central Bank of Europe would request for information with full justification. When there are objections by the addressees, they would still provide the information despite the objections. The decision would be taken by the European Union's Court of Justice in agreement with established procedures. Concerns associated with Central Bank's governance should be considered. Additionally, the European Banking Authority would have the leading role in the Single Supervisory Mechanism and it would be equipped with the necessary instruments in order to complete the tasks that it is responsible for. The members of the European Union would participate in the European Banking Authority with equal rights.

According to the Central Bank's supervisory tasks specified by the Regulation (EU) No 1024/2013, the European Banking Authority would have the responsibility to accomplish tasks which are related both to the Central Bank and the National Competent Authorities. More specifically, the current mechanism which settle the emergency actions and disagreements would be adjusted according to the needs of the particular situation in order to remain sufficient.

The European Banking Authority should be perfectly informed about the last developments in order to ensure its role as a facilitator and coordinator in case of emergency. Additionally, the National Competent Authorities would invite them to observe all the relevant meetings including the right to contribute accordingly or take the floor.

Furthermore, interests of the members are taken equally into consideration and consequently voting arrangements associated with the Board of Supervisors would be adapted in order for the European Banking Authority to function properly. An independent panel comprised of voting members from the Supervisors' Board would be responsible for any decisions associated with breaches of the regulations within the Union and the managing of incongruities. Most of the associates who vote within the Supervisory Board should implement the decisions made by the panel which would encompass a simple majority of National Competent Authorities of Member States participating in the SSM.

The Board of Supervisors should adopt decisions associated with emergency actions including a simple majority of the members from both competent authorities of participating and non-participating States. In addition, decisions associated with acts which are specified in the Articles 10 to 16 of Regulation (EU) No 1093/2010 and associated measures included in the third subparagraph of Chapter VI and Article 9 (5) of the particular Regulation should be adopted by the majority of the Supervisors of the Board along with a simple majority of its members from both National Competent Authorities of non-participating and participating members. Then, the European Banking Authority should create procedural rules for the panel which ensure its objectivity as well as interdependence (European Central Bank, 2013) .

Moreover, the Board Management would be composed of a proper and balanced representation of the Member States which do not participate in the Union and a geographical balance should be ensured for the appointment of the members of European Banking Authority committees and internal bodies.

The appropriate function of the European Boarding Authority as well as the depiction of all Member States would be ensured by the Management Board's composition, the administration of the independent panel' composition and the voting arrangements. These processes should be reviewed after a certain time period taking into consideration any developments and experiences that were relevant. Also, there would be no State that is a Union's member that would be discriminated as a place for fiscal services. The European Banking Authority should be equipped with the necessary fiscal and human resources providing support in order to accomplish any additional tasks (Official Journal of The European Union, 2013).

From an institutional view, the above Regulation has the potential to offer particular protection against any conflict of interests which may preserve the attitude of separation of the financial policy and supervisory role of the ECB. The grouping of the Central Bank's function and supervision in one institute permits particular precautions to eliminate reputational risk (European Central Bank, 2013).

Regulation (EU) No 1024/2013

Through Regulation (EU) No 1024/2013 the Single Supervisory Mechanism is recognized consiting of national authorities of the European Member States and the European Central Bank. The European Central Bank is recognized as the authority in charge for the sufficient running of the Single Supervisory Mechanism as well as for the functioning of the whole system. The Regulation gives the responsibility to the ECB to get involved in the credit institutions that are located in the Members of the European Union. Additionally, credit institutions, companies with financial holding, companies with mixed financial holding in EU members as well as branches of credit institution of EU members established in states outside EU, that are substantial, are supervised by the ECB.

National Competition Authorities have the responsibility for the supervision of institutions that are less substantial. The Central Bank would have an investigating section which would function independently. However, complete cooperation between the National Competition Authorities and the Central Bank is mandatory for the efficacious running of the Single Supervisory Mechanism. It must be guaranteed that the two institutions would exchange the necessary information that may influence the respective tasks of the Single Supervisory Mechanism.

The procedures are defined as well as time deadlines for the National Authorities' preparation of assertions for the Central Bank linked to the supervision of substantial as well as less substantial entities. There should be a report of the European Central Bank for the practice of the supervision and additional evaluation if demanded by the Central Bank as well as the communication of the supervisory decisions to the Central Bank where it would state its views.

Another domain where the Regulation establishes rules is information exchange and cooperation between the Central Bank and the Authorities of Member States at a national level concerning the procedures associated with the entities that are significant and less significant for supervision as well as the macro-prudential tools and tasks. According to the Article 1 of the Regulation, the Single Supervisory Mechanism cooperation must involve: “A specific methodology for the classification of a supervised institution as being more or less significant” (European Commission, 2015). In addition, further procedures that are regulated are related to the supervisory decisions adoption which is addressed to the entities supervised or other persons, the arrangements at a linguistic level between the Central Bank of Europe and National Competition Authorities as well as between the Bank and entities or persons which are under supervision. Finally, the Regulation does not influence the supervisory procedure and must be read together with Decision ECB.2004/2 and the Supervisory Board’s Rules of Procedure concerning decision-making in the Single Supervisory Mechanism (European Central Bank, 2014).

Regulation (EU) No 806/2014

The purpose of this Regulation is to give a structural definition of the Single Resolution Board. The Single Resolution Board is composed of a chair, a vice-chair and four members who are permanent as well as the authorities of the European Union countries which participate in the Single Resolution Board. Its operation is narrowed into the executive sessions in which those who participate are the chair and four members as well as permanent observers posed by the European Central Bank and the European Commission and the plenary session which consists of the full board. According to the Regulation the act is applicable to eurozone countries; however other countries can participate as well.

Some key points associated with the act are the definition of the Single Resolution Authority which is described as a Resolution Scheme put together by the board which should be approved by the European Commission in a crisis situation. In such a situation, the Scheme is going to be adopted in twenty-four hours presupposed that the European Commission does not have any objections. If the resolution scheme does not draw more than €5 billion from the single resolution fund, the decisions associated with it are taken in an executive board meeting comprised of the state authorities of the country whose bank is in a crisis. Then, the full board is the construction that takes the decisions (European Commission, 2013).

The Single Resolution Mechanism is a consultant structure which is comprised of the Single Resolution Authority and the Single Resolution fund. The Single Supervisory Mechanism together with the Single Resolution Mechanism comprises the basis of the European Banking Union and gives the supervisory tasks to the European Central Bank. The Single Resolution Mechanism is relevant to the Eurozone countries. However, other European Union countries have the right to contribute as well.

The tasks of the Single Resolution authority have the accountability of the banks which are under the administration of the European Central Bank. The board is in charge for the cross-border institutions as well as the largest ones which are under the direct supervision of the Central Bank. The rest of the banks are under the supervision and unswerving responsibility of the national authorities as well as the secondary responsibility of the Central Bank. The Single Resolution Authority starts when the resolution theme must employ the Single Resolution Fund.

The Act consists of the establishment of rules and procedures associated with the resolutions of banks and investment companies below the framework of a Single Resolution Mechanism and Fund. Other Acts related are the Regulation (EU) No 1024/2013 which is linked to the tasks of the European Central Bank connected to the banks' practical supervision policies, the "Regulation (EU) No 1022/2013" which establishes a European Supervision Authority and the "Regulation (EU) 2015/81" which stipulates the conditions where the "Regulation (EU) No 806/2013" is applied (European Central Bank, 2013).

The European Deposit Insurance Scheme

European Commission's proposal

The Banking Union plans were launched in 2012 after the sovereign debt crisis of 2008 had affected the global economy and forced European countries to offer 2 trillion euros in guarantees and capital in order to save the banks. After the agreement for common supervision for those that lend eurozone, the nineteen states of eurozone lost momentum and were stuck in the deliberations about the founding of European Deposit Insurance Scheme.

Nevertheless, on November 2015 there was an authorized proposal by the European Commission which modified the Regulation (EU) No 806/2014 to accomplish the establishment of a common insurance guarantee scheme.

According to the descriptive note of the proposal, the establishment of the European Deposit Insurance Scheme comprises of the third pillar of the Union of the European credit institutions in three sequential segments: a reinsurance scheme for national DGSs which participate in the union in an initial period of three years, a co-insurance scheme for the same group but this time for a second period of four years and full coverage for them in the steady state. A benefit from the European Deposit Insurance Scheme can be achieved only if the national DGSs have funds which are built up according to a specific funding path which complies with the fundamental requirements of the law of the Union. The monitoring of the national DGSs would be the responsibility of the Single Resolution Board which would release funds whenever it is well-defined that the conditions are met. The founding of European Deposit Insurance Scheme would be joint with procedures to eliminate risks in the financial sector of the members of the European Union.

The context of the proposal was the call of the European Commission for the creation of a Banking Union in 2012, a step that had the potential to reestablish confidence in the Eurozone as part of the general mission for financial integration. The employment of the Union should be accomplished by providing the supervision to the European Central Bank, creating a common framework for crisis management within the banking sector and a shared system for deposit fortification. The first two phases towards this direction are the founding of a Single Supervisory Mechanism and Single Resolution Mechanism and they have been already realized. Nonetheless, a common structure for the protection of deposits has not been implemented.

The report by the Five Presidents as well as the European Commission's response established a clear plan for the enhancement of the Economic & Monetary Union, encompassing movements to further eliminate risks to economic stability. The Banking Union would be the final step which would establish a complete and absolute Economic & Monetary Union. A completely integrated fiscal system is the key for the single's currency efficiency concerning the spread of financial policy, sufficient risk sharing within the Eurozone and wide-ranging confidence in the banking sector of Eurozone.

Predominantly, the repost of the Five Presidents recommends the establishment of a European Deposit Insurance Scheme in the longrun which would be the third prop of Banking Union along with the Single Supervisory Mechanism, which is accountable for the banks' supervision, and the Single Resolution Mechanism, which is accountable for the resolution of banks having been surrogated to the Single Resolution Mechanism.

The proposal is one of the first phases towards this direction with the purpose of creating a system which would be disconnected from the sovereign. The basic aim is the protection of the European citizens' deposits which would be independed from their geographical location. Additionally, the Commission clarified that the creation of a reinsurance oriented approach would assess the various subsidy levels of the state schemes as well as their ethical peril issues. The formation of a joint Deposit Insurance fund would be accomplished by the Single Resolution Board. Additionally, the Deposit Insurance Scheme would be domineering for the Members of Eurozone as well as the associates who wish to join the European Banking Union.

The "European Deposit Insurance Scheme" would progressively convert into a co-insurance scheme which would be fully mutualized in several years. This step is mandatory to eliminate the sovereign connections in certain Member States as the risk would be shared among them and consequently the Banking Union's objectives would be reinforced. Nonetheless, there would be measures that would reduce risk designated to stop the bank-sovereign relation in a direct manner (European Commission, 2015).

The Scope & Objectives

The scope of the European Deposit Insurance Scheme is associated with the determination of which Member States would be eligible for the provision of liquidity coverage. According to the proposal of European Commission, all banking institutions would receive the coverage. There is evidence according to which a shared system would function more sufficiently offering an increased level of shielding without needing to upsurge total contributions. Additionally, it would eliminate the states' exposure to their internal banking sector.

There are objectives with a potential positive outcome to the internal market, the shielding of the consumers and the fiscal stability in general (Five Presidents' Report Series, 2015).

The Stages for the establishment of EDIS

As mentioned earlier, there will be a phased development of EDIS – first a reinsurance arrangement and then an increasing level of co-insurance until full mutualisation is achieved. EDIS has the mission to address the fundamental need of the Member State to reimburse depositors within the disbursement deadline established by the Directive and please the call for involvement to an on-time resolution procedure. European Deposit Insurance Scheme would ensure losses by refunding depositors or getting involved in the resolution.

Reinsurance

The phase of reinsurance is intended to last three years during which EDIS would provide a limited funding and involves a distribution of the losses of the DGSs which is associated to a payout event or a contribution to resolution. At the beginning of this stage there is a limit related to coverage resolution proceedings which are arranged by the Board. However, proceedings associated with national resolution are covered by the next two stages.

The funding of this stage would be given in cases of a liquidity shortfall of the DGSs which participate. The procedure associated with it depends on the possibility of meeting a disbursement event by the DGS or the contribution to resolutions. If there is a disbursement event, the liquidity shortfall happens when the deposits which are covered within the fading bank is of larger amount than the amount of the financial resources available by the DGS. The amount of deposits which are covered and are employed to calculate the shortfall is comprised of eligible deposits which reach the amount of 100,000 euro or the equivalent amount of money in the national currency. The employment of the supposed amount of the available financial resources rather than the actual one has the potential to weaken the members' incentive to fall short of their responsibility to "raise ex-ante contributions in line with a precise funding path" (European Commission, 2015, p.10). At last, if ex-post contributions can be withdrawn within a short time period, they can become an additional means of liquidity that could reduce the shortfall of a Member State. A period of three days is the time during which the liquidity resources of the DGS should be exhausted. Then, the depositors should be paid in seven working days after the payout event.

The case of resolution is inspected in the Article 41 b (2) according to which liquidity shortfall consists of what the DGS which participate in the Banking Union have to offer to resolution. There is a hypothetical level of financial means which constitutes the sole financial resource that the DGS which participate in the EBU need to tap to eliminate any liquidity shortfall. In the case of resolution DGSs are not expected to offer more resources as according to the Article 10 (8) the DGS Directive is concerned only with the payout events.

In case the DGS experiences a liquidity shortfall, it may ask for 20% of the funds of the amount of shortfall. The rest 80% of the shortfall has to be covered by other resources. The application of the hypothetical financial resources that are available by each DGS allows the calculation of the liquidity shortfall of DGS permitted by the EDIS during the payout event. (European Commission, 2015).

In this phase, European Deposit Insurance Scheme has to provide the funding for the liquidity shortfall as well as an additional 20% of the DGS' additional loss. The concept of excess loss either refers to the payout events that DGS may encounter or its contribution to resolution. In the case of a payout event, DGS experiences an excess loss when the total amount that it gave to depositors transcend the amount that it had collected in insolvency proceedings on the claims of the deposits that it had obtained by paying back depositors.

When the liquidity shortfall is examined, the scheming associated with the excess loss that has taken place during the reinsurance stage can have its base on the amounts that have been given to the depositors. This sum is eliminated by the earnings from the liquidation state that the DGS has established. In addition, the supposed amount of the financial resources that are available by the DGS at the payout event is removed too. Finally, the DGS is supposed to have the capability to provide the amount of ex-post aids which is allowed to have by the DGS Directive within one year from the incidence of the disbursement event. This sum is equal to the 0,5 % of the deposits which have been covered by the banks that are associates of the DGS Directive with the aids which were withdrawn during the first three days after the disbursement. The amount that results comprises of the extra loss of the DGS.

According to the Article 41 in case of a resolution event, the extra loss comprises of the sum that the DGS has to provide to resolution. The sum may have been payed after a subsequent assessment which found out that its provision should have been lowered comparing to what was requested at a first place. Furthermore, the sum of financial resources that the DGS had available should have been provided by the funding solution which was established by Article 41. In this case, it is not necessary for the DGS to increase its ex-post involvement as the Article 10 (8) limits it to payout events. The application of the 20% of the excess occurs by eliminating the sum of funding which the DGS is obliged to give back to the European Deposit Insurance Scheme by the sum of loss cove (European Commission, 2015).

Co-insurance

Co-insurance is the subsequent stage which will take place after the completion of the previous stage which is expected to last three years. At this stage DGSs are co-insured by the European Deposit Insurance Scheme for a period of four years and have the right to ask for funding as well as loss cover from the Deposit Insurance Fund when they experience a payout event or have been asked to participate in the funding of a resolution. At this phase European Deposit Insurance Scheme is responsible for the provision of funding and the coverage of losses which come from the contributions to national resolution events. Furthermore, it provides the same amount of the loss the DGS ultimately experiences from the events stated. The percentage would be 20 % one year after the co-insurance stage and upsurges each year by 20 %.

When a disbursement event happens, the liquidity requirement is equivalent to the sum of deposits that are covered by the failing bank. When there is a resolution procedure, the liquidity requirement is equivalent to the sum of involvement that is asked by the Board and the resolution mechanism at a national level.

This stage is distinguished from the previous one regarding the subsidy that is provided as well as the damage that is covered by the European Deposit Insurance Scheme which will be augmented gradually.

Full Insurance

Following the co-insurance stage which is expected to last four years, the Member States will receive full insurance by the European Deposit Insurance Scheme. This stage offers full funding and covers all losses which come from payments or contributions to resolution events. The resolution mechanism is the same with the previous stages, while the only difference is that the European Deposit Insurance Scheme is responsible for the coverage of the total amount of liquidity needs.

However, in case that Member States do not comply with the responsibilities associated with the Regulations mentioned, they will be covered by EDIS only if their fiscal means are equal to the consistent fund path that is established by the Article 41j. This limitation is adopted to ensure that the Member States can comply with their obligations which eliminate the risks of reducing the liquidity of the European Deposit Insurance Scheme (European Commission, 2015) .

Oppositions to the creation of EDIS

However, there are Member States, mainly the more financially powerful ones, which disagree with the risk-sharing plans, based on the existence of many European countries with rotten banking sectors. These countries should clean up their banking sector in order to eliminate their systemic risk and then an agreement of all Member States would be probably reached. For instance, according to Germany, it is an urgent precondition that countries such as Italy and Portugal get rid of non-performing loans so as Germany places its money in shared funds to protect deposits and lenders from possible failures.

The European Commission decided to propose additional capital rules for the eurozone's lenders, incorporating tighter standards with the mission to make the banking system safer. Nevertheless, Germany as well as the Netherlands did not recognize the measures claiming that they are not enough to eliminate the risks and asked for tougher requirements. It is believed that the fragile Italian banking sector with the third biggest lender Monte dei Paschi di Siena which was entangled for long time to close a large capital shortfall made Germany more reluctant to approve plans of risk-sharing (Howard & Quaglia, 2016).

Similar oppositions were made by Danish political parties which claimed that they will seek for a referendum if Danish government decides to join the Banking Union. The parties which opposed to the Banking Union developments were the Eurosceptic Danish People's Party, the Red Green Alliance and the Liberal Alliance and all together were able to gain adequate seats to call for a referendum according to the political developments at a European level (Matzen, 2015).

Thus, a Banking Union is a part of long-term institutional framework which is not accessible because of problems of legacy. Hence, only intermediate solutions appear to be achievable. Direct banks' recapitalisation is partly the responsibility of national governments which have the liability for their banks resolution. According to a proposal by the German Council of Economic Experts, there was an advocacy for the "foundation of a Redemption Pact at a European Level" which would include a part of the liability of the states' sovereign debt which remains above the verge of 60 % when at the same time there would be an introduction of strict financial measures as well as a sovereign liquidation management. The common theme that is reflected is that the banking and the sovereign issues have to be resolved simultaneously as they are strongly interrelated (Buch and Weigert, 2012).

It is believed that institutional solutions as well as solutions associated to the ongoing financial crisis should be separated in order to transform the eurozone into a sustainable currency union. The way to achieve this goal is with the construction of the Banking Union. The employment of European deposit insurance may overshadow significant changes in the architecture of the European Union and introduce distributional conflicts associated with the resolution of the fiscal crisis.

The macroeconomic inequities in the European Union are the main issue that explains the desire of the northern European countries to protect their savings. It is suggested that the provision of a supervisory authority to the European Central Bank could have a significant impact that would allow the Single European Market to function and restart growing particularly in peripheral countries and hence reducing the consequences of financial policy.

There is an ongoing debate according to which the immense imbalances in the payment system of the Eurozone reflect the sponsoring of frail banks in southern countries by national banks which are financed by the target system. This funding of the banks without the necessary haircuts depicts the delay in addressing appropriately the bank fragility in southern countries. Therefore, a European Deposit Insurance would not be able to resolve imbalances, yet it needs to be accompanied by addressing the sovereign fragility effectively in peripheral countries (Beck, 2012).

Conclusions

After the financial crisis of 2008 in Europe, the need to address the weak aspects of the financial sector became urgent in order to reestablish the confidence of the investors and protect the citizens' deposits. The cost of the restoration of banks was especially high for the taxpayers, borrowers and depositors. As Draghi stated in 2013 when he was the president of the Central Bank, the crisis established the need for a common financial prosperity.

The creation of a Banking Union would shield the Eurozone area from potential risks, it would upgrade the Single Market and make the banks safer having the chance to offer access to financial resources which will be employed to achieve investments and growth. The trust will be rebuilt not only among European banking structures but also among the shareholders and the stakeholders.

The Banking Union is a goal associated with many legal issues that have to be solved. Considering that there used to be nineteen different supervisory mechanisms at a national level, everything seemed complicated. However, the first steps towards its implementation were made with the creation of the mechanisms of SSM and SRM: the two main pillars of the establishment of the European Banking Union. The former establishes the supervision procedures that the Central Bank of Europe provides and the latter the Resolution procedures that regulate the resolution of credit institutions within the Eurozone.

However, the third pillar, the European Deposit Insurance Scheme, still remains the missing piece despite the significant advantages associated with its implementation. With a purely national Deposit Guarantee Scheme, a large local shock is sufficient to leave depositors unprotected. A common European Deposit Insurance Scheme would have the potential to upgrade the capacity of national DGS to withstand local shocks and distribute the risks associated with "pay-out events" as well as resolution procedures. Consequently, there would be a more effective protection of the fiscal system and the financial market as well as citizens' deposits in case a domestic credit institution fails. During the last financial crisis in Eurozone, the majority of problems were experienced by the states with weaker banking sectors. Since that, the European Commission and the European Central Bank have passed several Regulations preparing the ground for the implementation of the EDIS, but have not achieve to finally implement it.

The reason behind this situation is the various oppositions that have been expressed by the more financially powerful Member States which fear that their contribution to the European Deposit Insurance Scheme would be higher. The risk-sharing model is not a popular idea for the citizens of Northern Europe who know that they would have to pay more for the southern problematic banks of European Member States. The high level of debt in Southern European countries as well as the non-performing loans is considered a threat for countries like Germany which perceive this idea as an attack to their citizens’ savings. However, Germany that is opposed to the establishment of a European Deposit Insurance Scheme will gain many benefits from a stable banking system as there would not only be risk sharing but risk reduction as well (Schoenmaker et al, 2016).

However, risks related to procedures that seem unclear and the inadequacy of information that is available for domestic banking sectors of each Member State lead to the inability of Eurozone countries to reach an agreement. Despite the evidence associated with the financial stability that the insurance scheme has the potential to offer, many countries are still not be able to pass the relevant regulations because of their voters’ oppositions to them.

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